Curtis C. Verschoor, CMA, Editor

Whistleblowers Need Encouragement, not Roadblocks

The Dodd-Frank Act expanded existing whistleblower programs, providing cash rewards for significant information given to the SEC. Despite these efforts to stimulate whistleblowing, companies are putting limits on how much (or how little) their employees can report fraud.

It's well understood that a whistleblower is the most important source of evidence in detecting fraud and other misdeeds and convicting the criminal or enforcing a civil statute. The whistleblower program at the U.S. Securities & Exchange Commission (SEC) has allowed many individuals to report securities laws violations. But companies and their counsel are reportedly impeding would-be whistleblowers in violation of the law. In addition, the Internal Revenue Service (IRS) and U.S. Commodity Futures Trading Commission (CFTC) whistleblower initiatives appear to require streamlining to improve their effectiveness.

The Dodd-Frank Act enables the SEC to pay cash to whistleblowers who report significant wrongdoing (more than $1 million in sanctions). In November 2012, then SEC Chairman Mary L. Schapiro reported, "In just its first year, the whistleblower program already has proven to be a valuable tool in helping us ferret out financial fraud. When insiders provide us with high-quality road maps of fraudulent wrongdoing, it reduces the length of time we spend investigating and saves the agency substantial resources."

The second cash award under the SEC's whistleblower program was announced June 12, 2013. The SEC will award three whistleblowers 15% of the total amount recovered by the government in return for tips and information they provided to help the SEC and the Justice Department stop a sham hedge fund. The total reward is expected to amount to approximately $125,000. Whistleblowers are paid from the SEC's Investor Protection Fund, which held more than $453 million at the end of the 2012 fiscal year.

Additional and larger awards are expected in the future. The SEC Office of the Whistleblower had posted 76 orders in 2013 (through August), each with monetary sanctions exceeding $1 million. These include well-known defendants such as U.S. technology company IBM, Dutch bank ABN AMRO, Swiss bank UBS Securities, and French oil company Total S.A. According to whistleblower attorney Jordan Thomas, "There has been a green line that financial services professionals have historically feared to cross, but they are now more willing to break their silence because of the SEC Whistleblower Program." He added, "In the coming years, I predict many of the SEC's most significant cases will be the result of whistleblowers who report their tips to the agency."

Obstacles

A court decision in Houston, Texas, involving General Electric (GE) may confound the protective rights of whistleblowers to be shielded from retaliatory acts of their employer. The plaintiff was a former executive at GE who alleged he was fired because he was a whistleblower. GE, however, claimed that the executive never reported it to the SEC, blurring the SEC's definition of a "whistleblower." The court stated that "without any allegation that he reported a securities-law violation to the SEC, [the plaintiff] is not a 'whistleblower' under Dodd-Frank." GE stated its "consistent position has been that employees should report internally first, with lawsuits and bounties reserved for instances where a company fails to

respond appropriately, obliging employees to report to the SEC." The plaintiff's attorney is contemplating an appeal to the U.S. Supreme Court.

The case hinges on the issue of whether the Dodd-Frank Act protects whistleblowers in general or just those who report misdeeds to the SEC. Several courts held earlier that all whistleblowers were covered under Dodd-Frank and thus were protected from reprisal. It appears that whistleblowers need legal representation to help determine the appropriate strategy, as recommended by the *IMA® Statement of Ethical Professional Practice*.

Another potential obstacle to the effectiveness of the SEC's whistleblowing initiative was pointed out in a May 8, 2013, letter to the SEC from whistleblower attorneys David J. Marshall and Debra S. Katz. They assert that "companies routinely include in separation agreements [restrictions] that undercut Congress' purpose in creating the SEC's whistleblower-reward program:

1. The requirement that the whistleblower renounce the right to receive any award the SEC might make as the result of a successful enforcement action; and
2. Requirements that an employee disclose to the company all past or future communications with any third party, including government agencies, and/or that the employee agree to cooperate with the company in any ensuing investigation by the SEC."

According to Marshall and Katz, companies continue to devise ways to restrict whistleblowers despite SEC rules stating that "no person may take any action to impede an individual from communicating directly with the Commission staff about a possible securities law violation." They continued, "The inclusion of such terms in severance agreements and settlement agreements resolving employment claims has a chilling effect on individuals who would provide information to the SEC about potential securities violations." The SEC's discussion of its Final Rule under Dodd-Frank Section 21F states that Section 29(a) of the Exchange Act (of which the Dodd-Frank Act is a part) specifically states, "Employers may not require employees to waive or limit their anti-retaliation rights under Section 21F."

In their letter to the SEC, Marshall and Katz noted that employees may not have legal counsel or much time to decide whether to sign a severance agreement favorable to their employer. In their view, such pressure undermines the protections from retaliatory acts that Congress and the SEC intended to afford whistleblowers. They recommend the SEC issue clarifying regulations "to stem the growth of an apparent effort to discourage whistleblowers from providing information to the Commission," which is the clear objective of the SEC's whistleblower reward program.

For guidance in applying the *IMA Statement of Ethical Professional Practice* to your ethical dilemma, contact the IMA Ethics Helpline at (800) 245-1383 in the U.S. or Canada. In other countries, dial the AT&T USA Direct Access Number from www.usa.att.com/traveler/index.jsp, then the above number.

More Encouragement Needed

The whistleblower program at the IRS revealed significant activity in its 2012 fiscal year annual report. There were 332 submissions, involving 671 taxpayers, that appeared to meet the statutory threshold of $2 million of tax, penalties, and interest in dispute. Awards of more than $125 million were paid during the year to 128 whistleblowers. In fiscal year 2013, the only publicly announced award under the revised 2006 statute was a payment of $104 million made to a former banker at Swiss UBS AG—the largest payment ever. The informant provided information that resulted in UBS turning over the names of thousands of Americans suspected of being tax cheats.

The IRS annual report raised concerns that it says need to be addressed to improve the whistleblower program:

1. Protection of whistleblowers against retaliation. There are no provisions similar to those in the Dodd-Frank Act.
2. Means of providing adequate protection of confidential information of taxpayers whose taxes are at issue.

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3. Clarification of the definition of "amount in dispute" and how to determine the amount of "gross income." Also, an observer may wonder why the threshold of IRS interest is $2 million rather than the $1 million in the Dodd-Frank Act.

In addition, on August 29, 2013, U.S. Attorney General Eric Holder announced a new program to encourage Swiss banks to cooperate with ongoing investigations of the use of foreign bank accounts to commit tax evasion. The Swiss government announced it would encourage Swiss banks to cooperate. "This program will significantly enhance the Justice Department's ongoing efforts to aggressively pursue those who attempt to evade the law by hiding their assets outside of the United States," Holder said.

The CFTC also has a whistleblower program initiated by Dodd-Frank, but no awards have been paid yet. During fiscal year 2012, the whistleblower office received 58 complaints and an additional 52 tips that weren't whistleblowers. The whistleblower office has created an educational program to raise awareness of its whistleblower program. Like the SEC, the CFTC has a Customer Protection Fund, which held approximately $100 million at the end of fiscal 2012.

Whistleblowing's importance to all professional accountants is further emphasized in a proposed revision to the international *Code of Ethics for Professional Accountants* published by the International Ethics Standards Board for Accountants (IESBA). An exposure draft titled "Responding to a Suspected Illegal Act" was released in August 2012 and has drawn 73 comment letters, including one from IMA. The objective of the new pronouncement is to "describe the circumstances in which a professional accountant is required or expected to override confidentiality and disclose the act to an appropriate authority."

As companies try to restrict whistleblowers while government agencies and organizations try to encourage and protect them, it appears increasingly important that whistleblowers follow the guidance contained in the *IMA Statement of Ethical Professional Practice*. It recommends that when dealing with the resolution of ethical conflict, you "consult with your own attorney as to legal obligations and rights concerning the ethical conflict." **SF**

Curtis C. Verschoor is the Emeritus Ledger & Quill Research Professor, School of Accountancy and MIS, and an honorary Senior Wicklander Research Fellow in the Institute for Business and Professional Ethics, both at DePaul University, Chicago. He is also a Research Scholar in the Center for Business Ethics at Bentley University, Waltham, Mass. He was selected by Trust Across America as one of North America's Top Thought Leaders in Trustworthy Business Behavior–2013. John Wiley & Sons has published his latest book, Audit Committee Essentials. *You can reach him at curtisverschoor@sbcglobal.net.*